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Weekly Commentary, Selected Financial Data, and Business Indicators

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Some Interest Rate Relief . . .

Just when expectations were becoming widespread that interest rates would turn upward as economic activity picked up and Treasury borrowings soared to new record heights, they did precisely the opposite. Paced by a full four percentage point drop in the Federal funds rate in less than 25 days, and fueled by a lowering of the Federal Reserve discount rate, short-term interest rates tumbled sharply. Even the banks' prime lending rate, riveted at 16½ per cent since last winter, responded, dropping by one-half of one percentage point. But although these developments may provide some respite to a recession-weary economy, they had better be savored while they last. For building on the horizon are a variety of ominous clouds which may not only preclude future interest rate declines—but may well send them spiking upward again before long.

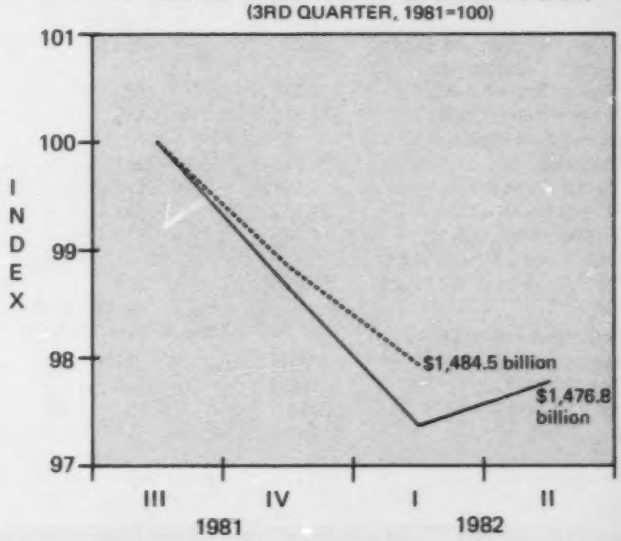
Perhaps the most threatening of these is the continuing clash between "tight" monetary and "loose" fiscal policies. Money supply growth has been sluggish at best in recent months, in spite of the well-publicized bulges which have occurred at the beginning of each quarter. During the 13 weeks ending July 14, for example, M1 declined at a 0.2 per cent seasonally adjusted annual rate while over the past month it has contracted at a more than nine per cent pace. Although there has been essentially no growth in the money supply since the turn of the year, it is just barely within the Fed's target ranges, thus not giving the Fed much leeway to loosen the monetary reins. Currently, M1 is about $750 million below its 5½ per cent upper target boundary and only $3.9 billion higher than the level reached in the first week of January.

For its part, fiscal policy remains highly stimulative, resulting in a huge and growing Federal deficit. And while there has been an apparent resolution of the fiscal 1983 Federal budget impasse, it has done little to assuage market jitters. Notwithstanding Congressional intent to keep the deficit to "only" $104 billion, the red ink total could reach as high as $120 billion in fiscal 1983, well beyond the record deficit expected for the current fiscal year.

. . . For A Recession-Weary Economy

This ensures that Washington's borrowing requirements will soar as well. Net new Treasury cash needs are likely to exceed $100 billion in the second half of this year alone, well above the $60 billion raised during the comparable 1981 period. Already, the borrowing pace is accelerating. In the first three weeks of July, net Treasury borrowings have surpassed $17 billion—$5.4 billion more than the net amount raised in all of the second quarter.

REVISED GNP (LINE) VS. EARLIER ESTIMATE (DOT)
(3RD QUARTER, 1981=100)



The persistence of these contradictory public policies, together with still robust business loan demand, suggests difficulties for the financial markets in general, and for interest rates in particular. If economic recovery does indeed become reality, the collision of Federal and private credit needs could send interest rates higher again later this year. And while a business upturn may slow the growth of short-term borrowings by boosting corporate cash flows, stepped-up household borrowings to finance a consumer-led rebound could take up the slack (notwithstanding the recent improvements in consumer cash flows and balance sheets). Simply put, there is still no way that an insatiable Federal credit appetite and monetary

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restraint are compatible with either stable or declining interest rates—unless, of course, the private sector remains flat on its back.

Statistical Quirks . . .

That may very well turn out to be the case. Although the rise in the second quarter's real Gross National Product was the first quarterly increase since last summer, it does not necessarily mean that a recovery is underway. The Commerce Department last week reported that the nation's output of goods and services increased at a seasonally adjusted annual rate of 1.7 per cent. However, closer examination reveals that, not only did the economy not strengthen, it may have actually weakened.

As it usually does at this time of the year, the government revised its figures going back several years. This time, most of the revisions were downward, especially for the period beginning in autumn, 1981. Whereas the Commerce Department earlier thought that fourth-quarter, 1981's GNP fell by an annual rate of 4.5 per cent compared with the third, it now thinks that the rate of descent was 5.3 per cent. Furthermore, first-quarter 1982's GNP is now shown to be down at a 5.1 per cent pace, compared with a 3.7 per cent clip previously. As a result, the level now estimated for second-quarter 1982's GNP—$1,477 billion—is actually lower than the government's earlier estimate for the first quarter, which was $1,485 billion (see chart).

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 7/14/82	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	140.798	– .243	+ 8.575
Loans to Depository Inst.	.558	– .514	– .739
Float	2.873	+ 1.246	– .420
Total Reserve Bank Credit	153.066	+ .003	+ 5.875
Treasury Deposits with Federal Reserve Banks	3.349	– .021	– .058
Currency Outside Banks	132.645	+ .656	+ 7.844
Member Bank Reserves:			
Required	38.957	– .257	– 1.551
Excess (Deficiency)	.165	– .375	+ .013
Total Reserves Held	39.122	– .632	– 1.538
Net Borrowed Reserves	.162	– .119	– .736
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	96.725	+ .529	+ .463
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates†			
M1	451.7	– 0.2‡	+ 4.8‡
M2 (June '82)	1,906.9	+ 8.9	+ 9.5
M3 (June '82)	2,294.7	+ 10.5	+ 10.2
L (February '82)	2,687.2	+ 8.8	+ 11.1

†Seasonally adjusted. *Seasonally adjusted annual rate. ‡Four-week moving average.

New York Money Market

Offering Rates 7/23/82	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	10.20%	10.00%	10.95%
* Federal Agencies	11.40	11.50	13.40
* Project Notes—Taxfree (46% Taxable Equivalent)	12.87	13.06	NA
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	12.00	12.60	13.38

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	10.00%	Aug.	10.80%
15- 29 days	10.50	Sep.	11.10
30- 59 days	10.38	Oct.	11.40
60- 89 days	10.75	Nov.	11.50
90-179 days	11.38	Dec.	12.00
180-239 days	11.13	Jan.	11.80
240-270 days	12.00		

‡Industrial Paper—Prime			
30- 89 days	10.88%	†Federal Funds Effective Rate	10.65%
90-120 days	11.50		

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'82n	$ 3,047	$ 2,996	$ 2,902
Gross National Product (1972 Dollars)*	2nd Q'82n	$ 1,477	$ 1,471	$ 1,502
Percent Change, Annual Rate	2nd Q'82n	1.7	– 5.1	– 1.5
Change in Consumer Prices (all urban consumers)*	Jun '82n	12.0%	12.0%	8.4%
Change in Producer Prices*	Jun '82	12.0%	0.0%	7.2%
Civilian Employment (Thousands of Persons)†	Jun '82	99,764	100,117	100,430
Unemployment as % of Civilian Labor Force†	Jun '82	9.5%	9.5%	7.4%
Personal Income*	Jun '82n	$ 2,561	$ 2,553	$ 2,398
Leading Indicators Composite Index (1967=100)†	May '82	127.7	127.3	136.0
Industrial Production Index (1967=100)†	Jun '82	138.4	139.4	152.9
Net Change in Consumer Installment Credit†	May '82	$ 1.40	$ 1.18	$ 1.57
U.S. Merchandise Trade Balance†	May '82	–$ 3.29	–$ 0.32	–$ 3.35
Plant and Equipment Expenditures*	3rd Q'82	$328.04(a)	$336.77(a)	$328.25
Private Housing Starts (Thousands of Units)*	Jun '82n	911	1,075	1,046
New Construction Expenditures*	May '82	$ 229.2	$ 226.2	$ 240.9
Total Business Inventories†	May '82	$ 505.7	$ 510.1	$ 490.3
Total Business Sales†	May '82	$ 349.0	$ 340.5	$ 349.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. a-Anticipated.

What is more, this "official" estimate for the level of economic activity in the second quarter is also below the level implied by the Commerce Department's "unofficial" estimate of mid-June. Although the quarter-to-quarter percentage increase is larger, the "unofficial" number was based on the higher estimates for the first quarter.

As if to underline this, the government one day later released its monthly report on durable goods orders for June. Not only was there a seasonally adjusted decline of 1.6 per cent for factory hardgoods, but there was an even heftier drop of 5½ per cent in new orders for nondefense capital goods—an important barometer of future plant and equipment spending.

In a similar vein, the Commerce Department revised downward its number for May. Earlier, it had estimated a 1½ per cent increase in May's new orders for durable goods; now it says there was a one per cent decline.

. . . Do Not Make A Recovery

Another factor contributing to last quarter's "rise" in the GNP was the adjustment for inventories. The way the GNP is put together, a step-up in the rate of stockpiling adds to it, while destocking subtracts from it. In the first quarter, real inventories were pared down by $15.4 billion at an annual rate, but in the second they were reduced by only a $6.9 billion rate. This moderation in selling from inven-

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Negotiable Time CD's Weekly Reporting Banks			
Nationwide (7/7/82)	138,201	– 721	+17,249
New York City (7/7/82)	35,039	– 357	+ 5,644
Commercial Paper (7/7/82)	181,597	+ 1,742	+32,734

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/7/82)	212,198	– 230	+30,125
New York City (7/7/82)	60,371	+ 503	+ 6,827

Total Loans Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/7/82)	490,079	– 784	+45,875
New York City (7/7/82)	115,132	+ 169	+ 8,718

Financial Markets

	Friday 7/23/82	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	10.72%	– .80	– 4.88
180-Day Bills†	11.80	– .62	– 4.20
Longest Bill†	12.40	– .49	– 3.30
Recent Issues:			
13¹/₈s 7/31/84 (When Issued)	13.12	NA	
14⁷/₈s 6/30/86	13.54	– .24	
13³/₄s 5/15/92	13.64	+ .51	
14s 11/15/11	13.29	– .02	
Municipals:			
Bond Buyer–20 Bond Index* (7/22/82)	12.01%	– .35	+ .67
Blue List Total ($ Million)	$ 782	– $ 27	– $130
30-Day Visible Supply ($ Million)	$2,607	+ $ 72	+ $932
Total	$3,389	+ $ 45	+ $802
Corporates:			
Moody's Aa Composite (7/22/82)	14.96%	– .33	– .16
30-Day Visible Supply ($ Million) ‡	$1,135	– $593	NA
Stocks:			
Dow-Jones Averages:			
Industrials	830.57	+ 1.90	– 106.17
Transportation	318.35	– 4.34	– 83.82
Utilities	106.45	– .92	– 1.12
65 Stocks	319.52	– 1.22	– 46.53
Standard and Poor's 500 Stocks	111.17	+ .10	– 17.27
N.Y.S.E. Composite Index	63.81	+ .14	– 10.79
N.Y.S.E. Avg. Daily Vol. for Week (000's)	56,436	– 7,390	+ 13,242

* 46% Taxable equivalent 22.24%.
‡ Series redefined: Historical data not available.
† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 7/23/82	Week Ago
Overnight	10.88%	12.75%
1 month	11.81	14.13
3 month	12.63	14.81
6 month	13.63	15.13
1 year	13.88	15.13
EURODOLLAR BONDS Average Yield		
Medium Term (5 to 7 yrs.)	14.40%	14.65%
Long Term (7 to 15 yrs.)	14.55	14.75

FOREIGN EXCHANGE SPOT RATES New York Opening (7/23/82)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02185	45.77
Canada	.7973	1.2543
Denmark	.1195	8.3655
France	.1498	6.6775
Germany	.4168	2.3995
Italy	.0007405	1350.40
Japan	.004009	249.42
Mexico	.02053	48.72
Netherlands	.3771	2.6520
Switzerland	.4942	2.0235
U.K.	1.7625	.5674

tories translated into an $8.5 billion "addition" to the GNP between the first and second quarters.

However, a slower reduction in inventories is not necessarily a sign of a stronger economy. This is because the most important indicator of economic activity—real final sales—declined in the second quarter by 0.6 per cent, paced by a 6.3 per cent annual rate drop in business fixed investment. The strong dollar and weak economies abroad contributed to a $1.3 billion decline in real net exports, compared with the January-March period, as the increase in exports was outpaced by even faster rising imports. Purchases of goods and services by the Federal and state and local governments fell by an annual rate of 6.3 per cent, quarter-over-quarter. The only component of real final sales which posted an increase was the consumer sector. Real personal consumption expenditures rose by 3.1 per cent at an annual rate, as the steep downturn in June did not offset stronger sales in April and May.

Nonresidential fixed investment declined for the second quarter in a row, dropping at a seasonally adjusted annual rate of 8.5 per cent, quarter-over-quarter. Not unexpectedly, this contraction in business expenditures occurred entirely in purchases of durable equipment. There has been little to encourage spending despite incentives provided by the Administration since early last year. Companies have been struggling with a downturn in sales (real final sales are no higher now than they were in the fourth quarter of 1980), excess inventories and the high cost of borrowing. These factors, coupled with a ten per cent cut in industrial production since last July, which has idled more than 30 per cent of capacity in the nation's factories, have all but eliminated the need for expansion.

The prospects for capital spending continue to be bleak. For example, the automobile industry, which intended to make sizable investments over the next several years, has been operating at less than 50 per cent of capacity. What is more, no sooner did the automakers pare inventories to healthier levels in May, than new domestic car sales slumped to 3.8 million units at a seasonally adjusted annual rate during the last ten-day selling period in June. This paltry selling pace has resulted in rising inventories once again, from a 52-day supply on June 1, to 78½-day's on July 1 at the then-current selling rate.

The sharp cutback in automobile production had severe repercussions on the metal producing industries, especially steel. Shipments to the automotive industry (including trucks) used to account for almost 25 per cent of all purchases; they now represent less than 18 per cent. In May, shipments of raw steel were down 30 per cent from a year earlier while total domestic production is now running at half the pace of a year ago. What is more, employment of hourly workers declined to 210,000—the lowest level since the Great Depression.

The problems of the steel producers have intensified this year because of the turnaround in the energy industry. Energy companies had earlier increased their demand for steel tubular products used in drilling for new oil. However, as prices of crude petroleum weakened, searching and drilling for new oil has become less attractive. This has resulted in plummeting drilling activity. As a consequence, investment in the petroleum industry, which had jumped by almost 50 per cent during the two years ending in 1981, is now falling rapidly. ■

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